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AN ANALYSIS OF SELECTED UNITED STATES
MARINE CORPS CONTRACTS INVOLVING
MINORITY OWNED SMALL BUSINESSES

by

HARVEY B. WILLIAMS III

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AN ANALYSIS OF SELECTED UNITED STATES MARINE CORPS CONTRACTS INVOLVING MINORITY OWNED SMALL BUSINESSES

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ABSTRACT

The purpose of this thesis was to examine difficulties associated with U.S. Marine Corps contracts awarded to minority owned small businesses under the 8(a) program. Specifically, causes of contract default and firm failure were identified; indicators which illustrated difficulties leading to default and firm failure were identified and steps which could have alleviated these difficulties and thereby prevented contract default or firm failure were recommended. A historical and legislative background for the 8(a) program has been developed. Six contract cases were examined in detail, in conjunction with a mail survey of USMC contracting officers and small business advocates, to determine the primary causes of contract default and 8(a) firm failure and their indicators. The thesis describes how observable indicators of contract default and firm failure can be recognized and how corrective action can be undertaken to significantly reduce the incidence of default and firm failure when dealing with companies participating in the 8(a) program.

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I. INTRODUCTION

A. GENERAL

Section 8(a) of the Small Business Act authorizes the Small Business Administration to enter into prime contracts with Federal Government procurement agencies and issue subcontracts for the performance of this work to small businesses owned and managed by economically and socially disadvantaged individuals. Due to their limited size, some important contracts awarded by Marine Corps Logistics Base (MCLB) Albany, GA qualify to be set aside for small businesses, particularly disadvantaged businesses under the 8(a) program. Although relatively small with respect to quantity and total price, the systems contracted for are technologically complex enough to cause small companies to assume a substantial amount of risk in contract performance. As a result of this assumed risk, these companies face a higher than average failure/default rate than larger businesses.

To ensure the success of Federal Government socio-economic goals associated with contract set asides, steps must be undertaken during the administration phase of contract performance to minimize company failure and contract default. This thesis will examine the difficulties associated with the administration of contracts awarded to firms under the 8(a)

program. Furthermore, the research will propose the actions the Government should employ to meet the goals the 8(a) program seeks to attain.

B. *OBJECTIVES OF THE RESEARCH*

The main objective of this thesis is to answer the primary research question: What steps can the Government take when dealing with 8(a) business concerns to prevent the firms from failing or defaulting on contracts that have been awarded? Secondarily, the thesis will answer the following subsidiary questions:

- What are the primary causes for failure or Termination for Default by small business firms relative to contracts awarded under the 8(a) program?
- What are the key indicators that an 8(a) firm is facing difficulties that could lead to failure of the company or a Termination for Default?
- What actions should the Government take to provide assistance to 8(a) firms in order to avoid failure or Termination for Default?

C. *SCOPE*

This thesis will provide the historical and legislative background for the Small Business Administration and the 8(a) program. An overview of the 8(a) program is provided followed by an examination of the program by the General Accounting Office (GAO).

The thesis will then provide a comprehensive examination of cases of 8(a) firm failure and Termination for Default. These case analyses are factual representations of recent contracts awarded under the 8(a) program by MCLB Albany, GA and illustrate specific examples of failed companies.

An analysis of information provided in response to a mail survey prepared for this thesis follows the case studies. The responses contain information pertaining to the primary causes of 8(a) firm failures and contract defaults. The responses also provide key indicators of potential difficulties which could lead to firm failure or Termination for Default. Steps to alleviate these difficulties are also provided. This information has been solicited from the contracting officers and small business advocates at the ten U.S. Marine Corps contracting offices and directorates.

D. *METHODOLOGY*

The background research material was collected from a literature review utilizing the Defense Technical Information Center, Defense Logistics Studies Information Exchange, the Small Business Administration, the University of California, Santa Cruz Library and the Dudley Knox Library at the Naval Postgraduate School.

The case summaries were derived from research performed at MCLB Albany, GA where contract documents were reviewed and interviews with cognizant contracting personnel were conducted. Telephone interviews with appropriate Defense

Contract Management Command (DCMC) representatives were also conducted to more accurately represent the conditions and circumstances surrounding each contract reviewed. Although discussions with company representatives for all of the contract cases was attempted, either no contact was possible or no comments were provided by the company representatives.

The mail survey of the USMC contracting officers and the small business advocates was developed to obtain a more broad based and generic summary of difficulties associated with the administration of contracts awarded under the 8(a) program. The survey population consisted of the ten contracting officers and ten small business advocates at the USMC contracting offices and directorates. After the surveys were completed the responses were collated and summarized in a tabular format. This representation of the information provides a sequential listing (in order from most common to least common) of the causes and indicators of contract default. Steps to alleviate these difficulties are also provided in the same manner.

E. ORGANIZATION OF THE THESIS

The thesis is composed of five chapters. Chapter I is an introduction to the thesis. Chapter II provides background, an overview and a summary of problems with the 8(a) program as a whole. Chapter III presents specific case summaries of contracts which were terminated for default and illustrates the causes of failure to perform; the indicators that

difficulties were being encountered and the steps which could have led to successful contract actions. Chapter IV summarizes and presents the information obtained from the mail survey, and Chapter V provides conclusions and recommendations based on all the information reviewed and analyzed during this research effort.

II. THE DEVELOPMENT OF THE 8(A) PROGRAM

A. HISTORICAL AND LEGISLATIVE BACKGROUND

In his book The Next American Frontier, Robert Reich provides a fitting introduction to a study of a socio-economic program. He writes:

> The way people work together to produce goods and services is intimately tied to the way they set and pursue public goals. This link is perhaps stronger today than at any time in America's past because we are moving into an era in which economic progress depends to an unprecedented degree upon collaboration in our work places and consensus in our politics....Americans tend to divide the dimensions of our national life into two broad realms. The first is the realm of government and politics. The second is the realm of business and economics. Issues of participation, equal opportunity and civil rights,...social security and welfare....are seen as aspects of government and politics. Issues of productivity and economic growth, inflation and unemployment, savings, investment, and trade are seen as aspects of business and economics--the substance of our business culture...In advanced industrial nations like the United States, drawing such sharp distinctions between government and market has long ceased to be useful. Government creates the market by defining the terms and boundaries for business activity, guided by public perceptions of governmental responsibility for the overall health of the economy. Business, meanwhile is taking on tasks that once were the exclusive province of government, involving responsibility for the work communities that are coming to be many Americans' most important social environment. The interwoven organizations of government, business, and labor together determine how America's resources are allocated and employed. Public and private spheres are becoming indistinguishable. [Ref. 1:p. 3-5]

The interwoven nature of the current procurement policies designed to implement socio-economic programs has been deeply rooted in the history of the United States from its earliest days. The Government of this country has been tasked with

significant responsibilities by the Founding Fathers through the Constitution:

> The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defense and general Welfare of the United States...To borrow Money...To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes...To coin Money, regulate the value thereof...To raise and support Armies...And To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof. [Ref. 2]

With this broad authoritative guidance as a basis to support the general welfare of the nation, our Government has implemented numerous administrative and legislative actions designed to advance the productivity of the economy and to enhance the standard of living of the citizenry throughout our history. In the early developing years, governmental regulation was extremely limited. Many of the early settlers came to America to avoid political and governmental oppression and favored minimal interference from the Government. "Apart from its role in developing early transportation systems, government was not critical to the first stage of America's economic evolution." [Ref. 1:pg. 7] Competition was viewed as the primary regulatory tool employed to insure that the national economy would progress satisfactorily. [Ref. 3:pg. 26] America was primarily an agricultural nation not relying heavily on industrial activity until about 1870. From 1860 to 1900 the value of this country's manufactured products surged from $1.8 billion to $11 billion annually in constant dollars.

The annual increase in productivity over the same period increased from .3% per year to over 1.8% per year--a sixfold increase. As businesses grew, more and more capital flowed into them. Unregulated and freewheeling, the growing businesses' productive capacity over ran the nation's ability to consume at a level high enough to support the fixed production costs generated by all the now large companies. [Ref. 1:pp. 23-32] Price competition ensued which forced many companies into bankruptcy. As these events occurred, monopolies developed which imposed severe burdens on consumers for required services and products. As a result, an era of governmental regulation began. [Ref. 4:pp. 55-57]

> The evolving American economy required systems of organization that could give it stability and legitimacy. Large, newly consolidated enterprises needed an institutional structure that could confirm their new role and help shield them against the ravages of the business cycle....And within society at large, popular acceptance of industrialization depended on a system of public administration to soften its social impact. [Ref. 1:p. 43)

The Interstate Commerce Act (1887) and the Sherman Anti-Trust Act (1890) were passed to usher in this era of regulation ending the long period of limited involvement in private business dealings. [Ref. 3:p. 28]

This early legislation was intended to provide a degree of protection to the general public from sharp and unethical business practices on the part of dominant corporations. During the first third of the twentieth century however, the legislation began to shift to promote the general welfare of the public and to increase the prosperity of the country.

[Ref. 5:p. 19] The Reconstruction Finance Corporation (RFC) was established in 1932 by president Hoover to restore the economy from the Great Depression. The Corporation had the backing of Congress and grew to provide many of the functions of the current Small Business Administration. [Ref. 6:pp. 3-9] President Franklin D. Roosevelt later provided his support for the shift as he stated:

> In our generation, a new idea has come to dominate thought about Government--the idea that the resources of the Nation can be made to produce a far higher standard of living for the masses if only Government is intelligent and energetic in giving the right direction to economic life. [Ref. 5:p. 19)

In conjunction with the RFC, additional agencies were established in support of this notion of advancing national prosperity and general welfare. The Smaller War Plants Corporation (SWPC), created by Public Law 603 on July 11, 1942, was the first Government agency to gain the authority to establish contracts with another Government agency so that it could award subcontracts to private businesses. It was established in response to difficulties encountered by small businessmen in competing for scarce wartime resources. Its purpose was to mobilize the productive facilities employed by small businesses to optimize wartime production. The enabling clause of the law was intended to insure small businesses would effectively and efficiently be used to produce supplies, equipment and material for both the war effort and for requirements in the civilian sector. [Ref. 7:p. 351] In addition to the authority to establish prime contracts with

other governmental agencies for the purpose of letting subcontracts to small companies, the SWPC was also granted the authority to provide loans to small companies so they could undertake these subcontracts. Public Law 603 provided the following language to support the authority for the SWPC:

> The Corporation is empowered...(4) to enter into contracts with the United States Government and any department, agency, or offices thereof having procurement powers obligating the Corporation to furnish articles, equipment, supplies, or materials to the Government; and (5) to arrange for the performance of such contracts by letting subcontracts to small business concerns or others for the manufacture, supply, or assembly of such articles, equipment, supplies, or materials, or parts thereof, or servicing or processing in connection therewith, or such management services as may be necessary to enable the Corporation to perform such contracts. [Ref. 7:p. 351]

The SWPC assisted in the award of 58,385 prime contracts worth $5.7 billion over a three year period which ended in November of 1945. Additionally, assistance was provided to various small companies so that they could also obtain over 52,000 subcontracts valued at approximately $30.6 million. Further, more than 5000 loans to small firms were granted providing over $500 million to small business enterprises. [Ref. 8:p. 5]

The Corporation did not exercise its authority to act as prime contractor on many occasions. Only twelve times did it enter into contracts with other Government agencies. These contracts resulted in about 260 subcontracts to small businesses valued at $35.5 million. [Ref. 8:p. 6]

At the end of World War II, the SWPC was abolished since its role had been conceived to expedite mobilization of the productive capacity of small companies in support of the war

effort. It had always been considered a temporary agency. Its authority and functions were transferred to the Department of Commerce and the Reconstruction Finance Corporation. [Ref. 8:p. 6]

It became clear that the Government had a substantial role to fill as the regulator of the economy in the United States.

> While the ideal of the 'free market' excluded planning, the series of economic crises and wars that marked the era had made planning organizations....central to the success of the American Economy. [Ref. 1:p. 57]

Following this line of reasoning, the House and Senate Small Business Committees, together with the Senate Committee on Banking and Currency were adamant in the belief that assurances providing for the welfare of small businesses were vital to the national defense. They voiced their opinion with dissatisfaction with the Defense Production Act of 1950 as it pertained to small business concerns:

> Experience under the Defense Production Act has demonstrated clearly the dangers to our free competitive economy and to independent small business....Constant vigilance must be exercised of all officials carrying out the program, to prevent undue concentration of industry and to prevent injury or destruction to innumerable independent small enterprises which frequently are less able to shift to defense production and less able to take care of themselves in a disturbed and partly controlled economy....Small business must be given a fair chance to bid or negotiate on procurement contracts; small business must receive fair consideration in the handling of applications for accelerated tax amortization and loans under title III of the act, small business must be fairly represented in the agencies administering the act and on advisory committees in those agencies, and the orders and regulations must provide for fair treatment and a fair distribution of materials for small business...Without this vigilant attention to the needs of small business, the mobilization program will suffer, their skilled labor force and managerial talents may be dissipated, and the

contribution which could be made by thousands of energetic and capable businesses would be lost. Equally important, in the long run perhaps more important, is the injury which will result to our free competitive economy unless small business receives full and fair consideration in all aspects of the mobilization program and is permitted to make its full contribution to the defense program. [Ref. 9:pp. 1597-1600]

Amendments sponsored by the House Small Business Committee to the Defense Production Act passed in 1951 established the Small Defense Plants Administration. The SDPA was given identical authority relative to taking on prime contracts from other Federal agencies and subsequently issuing subcontracts in their performance as was given to the SWPC. [Ref. 10:p. 130] The SDPA did not however, receive the authority to make loans. This responsibility fell under the purview of the Reconstruction Finance Corporation. Without the ability to provide loans to small businesses the SDPA's primary activity became the issuance of Certificates of Competency. [Ref. 8:pp. 3-7] In the short two year life of the SDPA the authority to take on prime contracts was exercised only seven times amounting to subcontracts with a total value of $2.3 million. [Ref. 8:p. 8]

In 1953 the SDPA and the RFC were abolished by the Congress with the establishment of the Small Business Administration (SBA). The SBA received the authority given to these two organizations in that it could both enter into prime contracts with other governmental agencies as well as issue loans to small businesses. The House Select Committee on Small Business illustrated the purpose of the SBA:

> That the Government should aid, counsel, assist and protect insofar as is possible the interest of small business concerns in order to preserve free competitive enterprise, to insure that a fair proportion of the total purchases and contracts for supplies and services for the Government be placed with small business enterprises, and to maintain and strengthen the overall economy of the nation. [Ref. 11:p. 2022]

With the passage of the Small Business Act on July 30, 1953, President Eisenhower emphasized his commitment to the value of competition and to the security, welfare and economic prosperity of the nation. This was illustrated by his agreement with the primary purpose of the SBA to encourage and develop both the actual as well as the potential capacity of small business to promote economic well being and realize national security. Section 8(a) of the Small Business Act provided the authority for the SBA to enter into prime contracts with other Government agencies thereby providing the SBA with the wherewithal to carry out its mission. The language contained in section 8(a) of the Small Business Act stated:

> (a) It shall be the duty of the Administration and it is hereby empowered, whenever it determines such action is necessary...
>
> > (1) to enter into contracts with the United States Government and any department, agency, or officer thereof having procurement powers obligating the Administration to furnish articles, equipment, supplies, or materials to the Government. In any case in which the Administration certifies to any officer of the Government having procurement powers that the Administration is competent to perform any specific Government procurement contract to be let by any such officer, such officer shall be authorized in his discretion to let such procurement contract to the Administration and the procurement officer; and

(2) to arrange for the performance of such contracts by negotiating or otherwise letting subcontracts to small business concerns or others for the manufacture, supply, or assembly of such articles, equipment, supplies, or materials or parts thereof, or servicing or processing in connection therewith, or such management services as may be necessary to enable the Administration to perform such contracts. [Ref. 12:p. 186]

Initially, the SBA did not exercise the authority given it by section 8(a). The section was viewed as a tool to be used in emergency situations:

> If all else fails, the administration may act as prime contractor itself. It is empowered to enter into contracts with other agencies of the Government having procurement authority and to circulate these contracts to small business firms...It is not expected that this power will be used extensively. It should, in fact, be employed only as a last resort. [Ref. 13:pp. 84-85]

The SBA felt that as long as a fair portion of the contracts generated by the Government were going to small businesses the legislation would not have to be expressly implemented. In 1958 the SBA declared that the authority to act as prime contractor was being officially placed on a standby basis. The authority was to be activated only in the event of an emergency situation. Additionally, the SBA stated that subcontracts issued under the authority of section 8(a) would be accomplished via solicited competitions and under standard procurement regulations. [Ref. 14:p. 12] Between 1958 and 1968 the 8(a) authority went unused and no mention of it appeared in the official reports of the SBA during the period.

The prototype of the present day 8(a) program was initially formulated under the Johnson Administration in 1968

to increase employment in the ghetto area of Watts in Los Angeles, California after the rioting of the mid sixties. The SBA awarded contracts to small minority companies in the Watts area, however, it did not reference section 8(a) in doing so. This activity of making noncompetitive awards did not have a statutory basis, but the SBA decided to ignore the provisions requiring solicited competition in these cases. [Ref. 15:p. K-3] The House Select Committee on Small Business became concerned due to complaints received that contracts which had been competed between small businesses were now being given on a noncompetitive basis to minority owned businesses under the 8(a) program. Although there was some disagreement within the committee regarding the statutory requirements, all agreed that the 8(a) program should not be used to take contracts away from other small businesses. [Ref. 16:pp. 15-38]

It became clear that if minority concerns were to be adequately represented by the SBA, statutory support would be needed. A series of Executive Orders were issued to provide assistance to minority enterprises.

Executive Order 11458 of 5 March 1969 established the Office of Minority Business Enterprise to coordinate plans, programs and operations within the Federal Government to contribute to the establishment, preservation and strengthening of minority owned businesses. All agencies of the Federal Government were to assist in the development of self-sustained minority business enterprises. [Ref. 17:p. 1]

Executive Order 11518 of 20 March 1970 provided that special emphasis should be granted within Federal departments and agencies as well as within the SBA to minority owned businesses. It indicated that particular consideration should be given relative to their needs in seeking entrance into the business community. [Ref. 18:p. 1]

Executive Order 11625 of 13 October 1971 prescribed further guidance in the development and coordination of a national program aimed at assisting minority owned businesses. Federal agencies were directed to foster minority business enterprise and to support ongoing Federal Government efforts in this area because:

> The opportunity for full participation in our free enterprise system by socially and economically disadvantaged persons is essential if we are to obtain social and economic justice for such persons and improve the functioning of our national economy. [Ref. 19:p. 1]

With these orders the president clearly indicated the direction the SBA was to take regarding assistance to minority owned firms. In the following years, however, Congress became dissatisfied with the lack of specificity and statutory authority resident in the guidance and with the resulting increased dependence on Government contracts minority owned firms developed due to the program. Public Law 95-507 was passed in October of 1978 to clarify the program's eligibility rights and to set forth the policy that:

> No small business concerns shall be deemed eligible for 8(a) program assistance unless SBA determines that, with contract, financial, technical, and managerial support, the small businesses will be able to perform contracts and have

> reasonable prospects for success in competing in the private sector. [Ref. 20:p. 14]

Public Law 96-481, passed on 21 October 1980, required the SBA to establish graduation dates for each company enrolled in the 8(a) program to clarify in greater detail that the program was designed to assist and develop minority owned enterprises to the point where they could compete in the procurement mainstream.

The terms of participation and the specific details of the 8(a) program have most recently been modified by the Business Opportunity Development Reform Act in November of 1988 (Public Law 100-656) and later by the Business Opportunity Development Act Technical Corrections Act in June of 1989 (Public Law 101-37). The Small Business Act and the 8(a) program in effect today have taken many years to evolve into their current form. An overview of the current 8(a) program follows to describe the environment contracting officers and minority businessmen work together in today.

B. AN OVERVIEW OF THE CURRENT 8(A) PROGRAM

The scope of the current regulations relative to the 8(a) program are put forth in 13 CFR section 124 with the following language:

> Sections 8(a) and 7(j) of the Small Business Act establish the Minority Small Business and Capital Ownership Development Program or 8(a) Program. The 8(a) Program is intended to be used exclusively for business development purposes to help small businesses owned and controlled by socially and economically disadvantaged individuals, economically disadvantaged Indian tribes...to compete on an

> equal basis in the mainstream of the American economy. [Ref. 21:p. 422]

The purpose of the program, to assist in the development of minority owned firms, is supported by section 8(a) of the Small Business Act as follows:

> Section 8(a) authorizes SBA to enter into all types of contracts, including, but not limited to, contracts for supplies, services, construction, research and development with other Government departments and agencies and to subcontract the performance of these contracts to small business concerns owned and controlled by socially and economically disadvantaged individuals, Indian tribes or Hawaiian Native Organizations. [Ref. 21:p. 423]

Section 124 of 13 CFR spans 66 pages detailing the particular definitions, procedures and requirements of the 8(a) program. The information which bears most significance has been summed up in a series of fact sheets published by the SBA which are made available to prospective businesses to provide key information without the legal jargon of the CFR. Fact sheet number 20 describes the Development Assistance 7(j) Program which authorizes the SBA to provide grants or loans to eligible recipients including "SBA's 8(a) certified firms, socially and/or economically disadvantaged individuals and/or firms and individuals or firms located in areas of high unemployment." [Ref. 22]

Fact sheet number 36 briefly outlines the 8(a) Program in easy to follow terms. The purpose and eligibility requirements of the program as they appear on the fact sheet are partially reproduced herein as follows:

PURPOSE

The purpose of the 8(a) Program is to:

(1) Foster business ownership by individuals who are socially and economically disadvantaged.

(2) Promote the competitive viability of such firms by providing such a viable contract, financial, technical and management assistance as may be necessary.

(3) Clarify and expand the program for the procurement by the United States of articles, equipment, supplies, service, materials, and construction work from small business concerns owned by socially and economically disadvantaged individuals.

ELIGIBILITY

Applicants for 8(a) Program participation must meet certain program requirements which include...

1. Ownership: In order to be eligible to participate in the 8(a) Program, an applicant concern must be one which is at least 51 percent owned by an individual(s) who is a citizen of the United States...determined to be socially and economically disadvantaged.

2. Social Disadvantage: Socially disadvantaged individuals are those who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities...

3. Economic Disadvantage: Economically disadvantaged individuals are socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities, as compared to others in the same or similar line of business and competitive market area who are not socially disadvantaged...

4. Control and Management: An applicant concern's management and daily business operations must be controlled by an individual(s) determined to be socially and economically disadvantaged, and such individual(s) must be engaged in the daily management and operation of the business concern... [Ref. 23]

Other details which are considered to be of particular importance which are not contained in the fact sheet have been summarized from 13 CFR section 124:

- Applicants for the program must demonstrate that they have been in business in the primary industry classification in which they seek 8(a) certification for two full years.
- Once a disadvantaged individual or the business concern he represents has exited the program due to termination, graduation, voluntary withdrawal or expiration of program term, he is not eligible to reapply for program participation.
- Each small business certified for program participation on or after 15 November, 1988, is subject to a program term of nine years from the date of certification. The program term consists of two stages, the developmental stage and the transitional stage.
- To remain eligible for the program an individual's net worth cannot exceed $500,000 in the developmental stage or $750,000 in the transitional stage. As part of the annual review participants must submit eligibility certificates, personal financial statements and a record of all payments.
- Participants must provide an updated business plan annually which outlines business targets, objectives and goals. The plan must contain an analysis of market

potential; an analysis of the participant's strengths and weaknesses; specific targets, objectives and goals for the next two years and estimates of anticipated awards regarding both 8(a) and non-8(a) contracts.

- The SBA is authorized to provide financial assistance for skills training by paying the costs of training or upgrading of employees or potential employees of 8(a) concerns.
- Although contracts in the 8(a) arena are normally awarded on a sole source, noncompetitive basis, competition thresholds do exist. If a contract designated for the program has an anticipated award price exceeding $5,000,000 for contracts assigned Manufacturing Standard Industrial Classification codes, or $3,000,000 for all other contracts, it will be competed among eligible 8(a) program participants.
- Participating firms must make substantial and sustained efforts to meet the non-8(a) contract targets of the business plan during the developmental stage. Firms must use the following table during the transitional stage to meet non-8(a) contract activity targets:

Program Year	Non-8(a) contract target (% of total)
5	15-25
6	25-35
7	40-45
8	50-55
9	65-75

Failure to meet these targets could result in remedial action such as requiring the participant to obtain managerial and technical training; conditioning the award of future 8(a) contracts on meeting the targets; reducing or eliminating sole source 8(a) contracts or program termination.

- Upon determining that an 8(a) firm should be graduated from the program, the SBA must notify the participant of its intent to graduate the firm in writing. The letter will outline the basis for the determination and will provide the participant 45 days to submit in writing any reason why the basis for graduating the firm is not warranted. [Ref. 21:pp.436-468]

It is clear that the 8(a) program is here to stay. Contracting officers must utilize minority owned businesses through the SBA for designated contracts. It is therefore essential that the program produce successful contract actions so that the procuring agency of the Government can receive the products it requires and that minority owned businesses can succeed and graduate from the program and stand alone to operate without preferential assistance from the SBA.

The program has received mixed reviews over its tenure. The WEDTECH scandal is well known as a major catastrophe of the program. This small, minority owned South Bronx machine tool company won $250 million in sole source, noncompetitive defense contracts under the program largely via payoffs and

bribery. [Ref. 24:p. 34] Shoddy workmanship and corrupt management eventually led the company into bankruptcy, but on the way they delivered faulty equipment to the Defense Department behind schedule and at extremely inflated costs. [Ref. 25:pp. 45-46] There are other problems associated with the 8(a) program as well. A careful examination of these problems can illustrate steps the Government can take to avoid difficulties in contract performance, prevent defaults and insure that scandals such as WEDTECH are a thing of the past.

C. SOME PROBLEMS WITH 8(A)

The General Accounting Office (GAO) published a report for the House Committee on Government Operations on 24 May 1988 entitled "Status, Operations, and Views on the 8(a) Procurement Program" in which it suggests that the program has done "too much for too few for too long." [Ref. 26:p. 1] The report addressed four key areas of the program: (1) a statistical overview of the program's participants, (2) concentration of contracting activity, (3) preparation of firms for the competitive market, and (4) adequacy of the SBA's administration and monitoring of the program. Additionally, GAO made a determination regarding how well 8(a) firms have met contract terms and conditions. Their findings are summarized from the report:

- Procurements from 8(a) contracts represented between 1.1 and 1.8 percent of total federal procurements in the six years ending 30 September 1987.

- From the program's beginning in 1968 through the end of fiscal year 1987, 1,287 firms had graduated from the program. Of these, 76 percent had graduated between 1985 and 1987. This concentration of graduates is due to Public Law 96-481 which required the SBA to establish graduation dates for each firm. Additionally, as of 30 September 1987, 72 percent of the participating firms had been in the program five years or less. These statistics indicate a high recent turnover rate in the program.
- Contracting activity was found to be highly concentrated. In 1987, the top 50 firms received 35 percent of the total dollar value of 8(a) contracts awarded. On the other hand, 39 percent of the active 8(a) firms did not receive any 8(a) contracts that year, and 17 percent received $100,000 or less in 8(a) business. "In other words, over 55 percent of the active 8(a) firms received less than 1 percent of the 8(a) business, and less than 2 percent of the firms received over 35 percent of the 8(a) business."
- The review indicated that 8(a) firms were not being prepared for the competitive market. Nearly one third of the firms that graduated between October 1982 and February 1986 were no longer in business. In response to a questionnaire, 58 percent of 8(a) business owners indicated that graduation from the program had a

devastating effect on their business. Regarding the firms who had been in the program for seven years, which at the time of the report was their last year of eligibility, 8(a) sales represented at least 90 percent of the revenue for 30 percent of the firms; 52-87 percent of the revenue for 42 percent of the firms; and less than 50 percent of the revenue for only 28 percent of the firms. Another indicator that self sufficiency was not being developed came from the sales growth of 10 of the top 50 firms enrolled in the 8(a) program in the five years before the end of fiscal year 1987. Over 75 percent of the growth of these firms came from 8(a) sales. "Collectively, the 10 firms' dependency on 8(a) sales decreased from an average 82.6 percent to 81.3 percent during the five year period. Individually, however, six of the ten firms were more 8(a) dependent in their last year."

- The GAO contended that the SBA's procedures for encouraging non-8(a) business and developing 8(a) firms into self sufficient enterprises were not being complied with. The GAO found that the files at the SBA did not indicate that required annual reviews had been conducted in 108 of 142 firms. The files did not contain evidence that required site visits were made for 122 of the 142 firms. The files also did not

contain evidence that required annual financial statements were received for 57 of the 142 firms.

- In response to these and other findings, the SBA indicated that district offices do not have the staff necessary to conduct all required reviews and site visits. The SBA contended that the files do not adequately represent the extent of SBA contact with 8(a) firms and that the interests of 8(a) firms take precedence over strict adherence to 8(a) support requirements.
- The GAO report found that in general 8(a) firms who received awards under the program performed satisfactorily. This determination was based on a mail survey of Federal contracting officers administering 478 open and 366 closed 8(a) contracts. The survey indicated that for about 85 percent of the contracts, 8(a) firms performed as well as non-8(a) small businesses, but that about 37 percent of these contracts were judged to be more costly to the Government. One half of the contracting officers surveyed indicated that 8(a) firms required more or much more monitoring than non-8(a) firms, while the other half indicated 8(a) firms required similar monitoring as other firms. [Ref. 22:pp. 10-25]

The concentration of contracting activity; the preparation of firms for the competitive market and the

adequacy of the SBA's monitoring of the program are areas on which the SBA must focus its attention to resolve. The contracting officer must focus on contract administration once an award has been made by the SBA to ensure successful contract completion. Using hindsight, a close examination of the causes of contract default can reveal the indicators which signal that difficulties in performance are occurring which could lead to default. Once these indicators have been identified, corrective action can be initiated by the contracting officer administering the contract to resolve the difficulties and prevent potential default. A review of six contracts between MCLB Albany, GA and minority owned firms follows to illustrate in specific terms the causes and indicators of contract performance difficulties encountered in recent contracts as well as the steps available to alleviate them.

III. CONTRACT CASE SUMMARIES

A. INTRODUCTION

The following cases have been summarized based upon information obtained from research conducted at MCLB Albany, GA during the week of 7-12 July 1991. Although the names of contractors in these cases have been changed, and modifications made where necessary due to pending litigation or termination negotiations, these cases represent current and factual contract situations. The information was compiled from the contracts themselves, attachments and memorandums appended to them as well as from interviews with cognizant contracting personnel familiar with the details and circumstances associated with the contracts. Each summary follows the same basic format as follows:

- AN OUTLINE OF THE REQUIREMENT CONTRACTED FOR
- A BRIEF DESCRIPTION OF THE CONTRACTOR(S)
- A SUMMARY OF THE DETAILS OF THE CONTRACT(S)
- A SUMMARY OF THE CIRCUMSTANCES ASSOCIATED WITH THE PERFORMANCE OF THE CONTRACT(S)
- AN IDENTIFICATION OF THE SPECIFIC CAUSE(S) OF DEFAULT
- A SUMMARY OF THE INDICATORS WHICH WERE OBSERVABLE DURING PERFORMANCE WHICH PRECEDED THE PENDING DEFAULT
- A SET OF RECOMMENDATIONS WHICH COULD HAVE BEEN TAKEN TO ALLEVIATE THE DIFFICULTIES

In most cases the writer believes it is extremely probable that the recommended actions would have resulted in successful

contract actions, had they been implemented appropriately and in a timely manner.

Table I below describes the cases which follow to illustrate which requirements are associated with a particular contractor. Two contractors listed for a single requirement is an indication that the first contractor listed failed to complete the contract and the second contractor was awarded a subsequent contract for the same requirement. More than one requirement associated with one contractor is an indication that this contractor had more than one active contract at the time of default.

TABLE I
CONTRACT CASES

CASE	REQUIREMENT	CONTRACTOR(S)
1	COMPUTER SYSTEM DEVELOPMENT	MENDON INDUSTRIES
2	AN/PRC-68A RADIO SET	TOWSON ELECTRONICS OKLAHOMA RADIO
3A	BASIC ELECTRONICS MAINTENANCE TRAINER (BEMT)	CREATIVE CONCEPTS FERRIS INTERNATIONAL
3B	TEAMPAC MAINTENANCE TRAINER	FERRIS INTERNATIONAL
4A	GUARDIAN ARMOR/ARTILLERY SIMULATOR	DEDALUS INCORPORATED
4B	COBRA HELICOPTER SIMULATOR	DEDALUS INCORPORATED

B. CASE 1

THE REQUIREMENT

This contract was initiated to upgrade the computer system used in the office of the project manager for training devices (PM TRADE). The system being utilized was technologically antiquated, slow and not user friendly. As a consequence it was underutilized and lacked the capacity to provide optimal project management support. The statement of work required Mendon Industries to evaluate the system in place and develop a more effective and efficient system, place it in service and provide a 90 day demonstration and evaluation period. The new system had interface, capacity and speed requirements detailed in the specifications and had to contain a user friendly tutorial package. This effort was to be implemented in the offices of three project directors as a prototype system with the potential for implementation throughout PM TRADE.

THE CONTRACTOR

Mendon Industries is a minority owned firm based in Falls Church, Virginia with a branch office in Clearwater, Florida where this contract was to be performed. Mendon Industries had previously demonstrated managerial competency and technical ability to both the Small Business Administration and other Government agencies from whom it had previously received contracts, thereby earning a reputation as a reliable and capable firm. As a result, the company received a significant amount of business under the 8(a) program. This

particular contract was relatively small in monetary terms in comparison with the company's other Government work, which came from a variety of Federal agencies, however the contract option for wholesale implementation of the system made the contract particularly attractive to the company. The firm was capable in areas such as software development and management, ADPE configuration management, systems interface as well as the integration of specialized hardware into unique systems.

THE CONTRACT

A Firm Fixed Price contract was issued in the amount of $94,276 in March of 1990. This price was negotiated from the contractor's original proposal of $136,567. The contract contained an option for installation throughout PM TRADE amounting to $4.5 million. The original discussions between the technical representatives at PM TRADE and the contractor's engineers and contracting personnel were conducted assuming a proposed Time and Materials contract with relatively imprecise specifications would be issued. Shortly before the negotiations however, the specifications were rewritten in sufficient detail to allow for the utilization of a Firm Fixed Price contract concisely outlining the requirements of the statement of work.

THE SITUATION

At the time this contract was issued, MCLB Albany, GA had another active contract with Mendon Industries and had experienced previous successful dealings with the company. Contract costs tended to grow with this company as the preceding Time and Materials contracts progressed because the company was able to expend more costs in contract performance due to the vague and imprecise language contained in the specifications. The Government had not been able to accurately definitize the specifications in earlier and pending contracts. In this contract, however, in an attempt to effectively control costs, great care was taken to definitize and precisely structure the specifications, effectively limiting the contractor to the price agreed upon. The contractor had initially drafted his proposal for another Time and Materials contract for the system which would have provided him a significant degree of program flexibility, but when given a fixed price requirement, the company lost this flexibility and did not adequately adjust the price for the increased risk associated with a Firm Fixed Price contract.

As the contractor completed initial preparations to begin working on this contract it was evident that the negotiated price was insufficient and that profits would be minimal or a moderate loss could occur. Additionally, options for other Government work were subsequently exercised which effectively maximized the productive capacity of the firm. As a result,

Mendon Industries failed to initiate the project by the start of work date. In the weeks that followed, progress reports lacked concreteness and specific milestone attainment status. The contracting officer's technical representatives indicated that the reports contained data which were based on projections and planned activities with no substance. After 60 days, the contracting officer called a meeting with the contractor to discuss the lack of significant progress on the project. At this meeting the contractor presented vague generalities and elaborate graphics of planned implementations and improved technology without specific accomplishments. After the meeting the contractor was given 30 days to make substantial progress. After 30 days when no progress was apparent, the contracting officer notified Mendon Industries of their default status and that the options on this and other pending contracts would not be exercised.

It was clear that the company had the ability to perform this contract, but was overcommitted to other Government work. This contract represented minimal profits or a potential loss so the contractor hoped for a Termination for Convenience, and to renegotiate a subsequent contract that would incorporate technological improvements in the specifications. The contracting officer became aware of the contractor's desires but felt that completion of this contract was in the best interest of the Government. A 90 day extension was negotiated, with the improvements cited above provided as

consideration. Mendon Industries devoted sufficient resources to make minor progress on the contract, but still failed to meet the delivery schedule as modified. The company was clearly in a default status at this point in time, however the contracting officer believed continuation of this contract was in the best interest of the Government. Two additional 90 day extensions were necessary and aggressive technical representative monitoring was instituted to insure adequate completion. Additional consideration was provided in the form of increased processing speed and an additional 60 day evaluation period of the prototype system. Although this contract was not terminated, the additional costs from delay and excessive contract administration made this a difficult and burdensome program to manage for the Government and an unprofitable endeavor for the contractor.

THE CAUSES OF DIFFICULTIES

This small company did not have experience in Firm Fixed Price contracting. The proposal which was submitted and the agreement which was negotiated did not provide for the actual costs incurred. The company was not prepared for the restrictive price of a Firm Fixed Price contract and was overcommitted. With options pending on other Government contracts so close to the start date of this contract, the company assumed a great deal of risk by accepting this contract. Furthermore, Mendon Industries did not have the financial or personnel resources to perform all of its requirements.

THE INDICATORS

There were two indicators that the proposal was not carefully drafted. The first was that the price for the Firm Fixed Price contract was the same as that planned for the Time and Materials contract. Secondly, after the change from Time and Materials to Firm Fixed Price, the new proposal was submitted in less than one week. The contractor had not been exposed to Firm Fixed Price contracts for this type of work and did not take the time needed to fully assess the rigorous price aspect and risk associated with the Firm Fixed Price contract.

The overcommitment of the company's resources was indicated in three ways. The first was the late start on the project. This was followed by the incomplete and insufficient progress reports which contained technical language without specific accomplishments. The third indicator, again related to the first two, was the vague responses given by the contractor at the meeting called by the contracting officer after the initial 60 days of contract performance.

RECOMMENDED ACTIONS

Although the contract was ultimately performed, extensive effort was required on the part of the contracting officer and the contractor. A more thorough examination of the contractor's workload prior to award could have resulted in an award to another capable firm which would have successfully performed the contract. The requirements of the statement of

work were not extremely difficult; many other 8(a) firms were qualified to perform them. Pre-award actions could have prevented post-award difficulties.

With respect to the proposal, the contracting officer should have recognized the increased risk in Firm Fixed Price contract performance and negotiated a more fair and reasonable price to alleviate some of the risk of loss for the contractor. This increased funding incentive would probably have encouraged Mendon Industries to devote its assets to this contract in a more timely manner. The contracting officer should have also extended the solicitation period and encouraged the contractor to reevaluate his proposal in light of the new contract type.

Action on the lack of progress should have been initiated earlier. By waiting 60 days the Government relinquished some of its rights associated with requiring the contractor to strictly conform to the schedule. This initial period indicated that the Government would not require the contractor to rigidly meet the milestones of the schedule. With this precedence set, the contract was subject to multiple extensions with little consideration. Had pressure been applied early in this contract a more substantial portion of the company's resources would probably have been devoted to this contract as opposed to the company's other contracts.

C. CASE 2

THE REQUIREMENT

The two contracts described below were entered into to acquire a total of 7939 AN/PRC-68A radio sets. This radio is a small, hand-held, short range VHF-FM receiver/transmitter used by United States Department of Defense forces for small unit (squad/platoon level) command and control. The 68A version is a product improvement model of the original AN/PRC-68 radio set. The requirement for these radio sets represents the quantity required to outfit the prepositioned war reserves (PWR) at MCLB Albany, GA and to complete the outfitting of active Marine forces with the improved model radio.

THE CONTRACTORS

Towson Electronics is a minority owned firm located in Baltimore, Maryland. The company lacked experience in contracting for military requirements, which require an approved quality assurance plan and a communications security (COMSEC) material systems account. The performance of this contract required the obtainment of these things as well as extensive tooling, special test equipment and other Government Furnished Equipment (GFE). Further, the contractor needed to expand his capacity to perform this contract.

Oklahoma Radio is another minority owned firm located near McAlester, Oklahoma. The contractor's business base is heavily dependent on Government contracts, both competitively won and issued under the 8(a) program. Commercial contracting

activity represented only a minor and insignificant portion of the firm's efforts. The company had historically been extremely dependent on progress payments and had been marginally solvent throughout its 20 year history. Despite these financial weaknesses the company maintained exceptional quality control and produced excellent products. The owners of Oklahoma Radio regularly replaced the upper level management after short periods of time. Six months to one year had been standard tenure for these officials. In 1989 after significant losses were reported on the financial statements, the company reorganized and sold stock to its employees making it an 85% employee owned enterprise and postponed the firm's subsequent bankruptcy until May of 1991.

THE CONTRACTS

In September of 1986 a $4 million Firm Fixed Price contract was awarded to Oklahoma Radio by Headquarters, United States Marine Corps (HQMC) for 3081 AN/PRC-68A radio sets. The contract contained an option to purchase an additional 3500 radio sets in the following year.

In April of 1989 a $1.9 million Firm Fixed Price contract was awarded to Towson Electronics for 1257 AN/PRC-68A radio sets to satisfy additional requirements which arose after the Oklahoma Radio contract and to establish a second source to enhance logistical support and increase industrial preparedness, thereby promoting combat readiness. This contract was also awarded by HQMC. Subsequent to the award of

this contract both contracts were transferred to MCLB Albany, GA on 9 May, 1989.

THE TOWSON ELECTRONICS SITUATION

Although awarded after the Oklahoma Radio contract, an examination of the Towson Electronics contract first is appropriate since after default the requirement for the 1257 radio sets was awarded to Oklahoma Radio in addition to its already existing contract and options.

First article testing of the radio sets from Towson Electronics was scheduled to commence 180 days after contract award. Since the radio set had been in production for three years, the manufacturing requirements were very straightforward posing minimal risk for the contractor. Production deliveries were required nine months after first article test approval. This represented a realistic schedule for both the contractor and the Government. The contractor was initially required to obtain a COMSEC account number within 45 days after contract award, however this time frame was revised to 90 days at the 14 June 1989 post-award conference. The contractor was also required to have an approved quality assurance plan within 30 days after contract award (24 May 1989).

After the post-award conference on 14 June 1989 a technical representative from the weapon system manager's office gained access to the production facility in use by Towson Electronics for the AN/PRC-68A radio sets. This

particular facility contained no tooling, machinery, materials, vendor parts or other indication that production was underway or even planned. At this point it was evident that the contractor would probably not meet the scheduled first article test date.

On 9 August 1989 the contract administrator at Towson Electronics informed the contracting officer at MCLB Albany, GA that the DCASMA, Baltimore quality assurance representative (QAR) had rejected the contractor's quality assurance plan ten days earlier on 30 June 1989. According to the Towson Electronics contract administrator, the QAR stated that the inspection requirement included in the statement of work (SOW) differed from that shown on the contract data requirements list (CDRL), and until this discrepancy was resolved, there would be no Government review of the plan.

On 16 August 1989 the quality assurance manager at Towson Electronics wanted to review the parts lists and drawings which were provided to the contractor upon award of the contract. On 18 August 1989 Towson Electronics asked for authorization to obtain the tooling required by the contract. The company was informed that the contract was the necessary authorization to obtain the tooling.

On 23 August 1989 the ACO informed MCLB Albany, GA that a DCASMA, Baltimore team had visited the Towson plant on 9 August 1989 and was concerned about the status of the contractor's performance. The ACO indicated that Towson

Electronics had not yet placed any orders for parts; the schedule for first article test was in serious jeopardy and the contractor had not yet obtained a COMSEC materials account number. Two days later the ACO called back and indicated that the contractor still did not have an approved quality assurance system in place and that there was no production in process in the plant on any Government contracts.

A Cure Notice was issued on 30 August 1989 based on anticipatory repudiation of the contract for the following reasons: (1) no orders had been placed for vendor parts; (2) notification by the contractor to the ACO that the first article test date would be delayed; (3) the contractor did not have an approved quality assurance system in place and (4) the contractor had not yet obtained a COMSEC materials account number. The contractor responded to the Cure Notice on 5 September 1989. Statements made by the contractor as a result of the Cure Notice and the Government's responses were as follows:

Contractor: Necessary changes to the contract were identified at the post-award conference (PAC) and the contractor was advised not to proceed until the contract had been modified.

Government: Changes discussed at the PAC involved an extension in the due date of the COMSEC account number from 45 to 90 days after contract award and changes to the data list addressees due to the change in procuring offices. These

changes were all minor and had no impact on the contractor's progress. The contractor was not directed to not proceed.

Contractor: The DCASMA Baltimore QAR had refused to review CDRL item B001, quality assurance plan, due to the discrepancy between the SOW and the CDRL.

Government: MCLB Albany, GA was not notified of this fact until 9 August 1989, and CDRL item B001 was due 24 May 1989.

Contractor: Towson Electronics encountered problems in obtaining the special tooling from vendors.

Government: MCLB Albany, GA was not informed there was a problem until 18 August 1989, (almost four months after contract award). Letters were issued by the PCO dated January 1988, in the solicitation phase of the procurement, authorizing the special tooling vendors to provide quotes to potential bidders since the tooling was to be Government property. The contractor needed the quotes from these vendors in order to prepare his bid or should have put the Government on notice immediately that there continued to be a problem.

Contractor: Only two orders for parts were submitted due to the special tooling problem.

Government: The contractor stated in the pre-award survey (PAS) that they would order all materials for the contract at one time upon award of the contract. They have not complied with this statement. Giving the special tooling problem as a reason for not doing so is not valid. All material required on this contract is not special tooling. Additionally, the

contractor did not provide notice of any problem with materials until four months after contract award.

Contractor: The Government furnished equipment (GFE) radios were not delivered on time, and were the wrong configuration.

Government: The GFE radios were received by the contractor on 31 May 1989 (seven days past the due date). The contractor was never instructed to use these radios for configuration guidance as the technical data package (TDP) governs configuration. The GFE radios were subsequently replaced by the latest version currently being produced under another contract at the request of the program manager, for informational purposes only. The new radios had absolutely no impact whatsoever on configuration, nor did they effect the contractor's manufacturing or purchasing processes.

Contractor: A long and tedious process of configuration identification had to take place prior to placing orders for material.

Government: A competent bidder would have thoroughly reviewed the TDP prior to submitting its bid, not after contract award.

Contractor: Material leadtimes precluded the contractor from being able to meet the first article test schedule.

Government: Leadtimes were known at the time of the PAS. The contractor had stated all materials would be purchased upon contract award, and the Government was not notified in a timely manner of any problem affecting vendor parts.

Contractor: The Chief Executive Officer of Towson Electronics submitted the company's application for the COMSEC account number on 18 May 1989.

Government: The COMSEC account number has still not been issued in accordance with the requirements of the contract.

Contractor: The DCAS QAR cannot complete the review process of their quality assurance system because they are not in a production mode.

Government: The contractor should already have been in production of the ten first article test units prior to submission of their quality assurance plan, in accordance with their own milestone schedule.

The contract was terminated for default on 22 September 1989 for the reasons set forth in the Cure Notice. Termination negotiations found the contractor at fault, but lack of timely action on the part of the Government in conjunction with extensive petitioning from Towson Electronics' legal counsel regarding the circumstances noted in the response to the Cure Notice prompted the Government to convert to a Termination for Convenience in January 1990.

THE OKLAHOMA RADIO SITUATION

The following represents the major awards/options exercised relative to this contract:

DATE	QTY/CUM QTY	DOLLAR VALUE/CUM TOTAL
SEPTEMBER 1986	3081/3081	4M/4M
MARCH 1987	3500/6581	3.7M/7.7M
OCTOBER 1989	1257/7838	1.9M/9.6M
FEBRUARY 1990	101/7939	.3M/9.9M
ECP'S AND SPARES 1990-1991		.3M/10.2M

The original award of 3081 in September, 1986 was followed by exercising the option for 3500 on the same contract in March, 1987. The contract for the 1257 from Towson Electronics was awarded in October, 1989 followed by an additional award of 101 in February of 1990. Additional requirements raised the value of the contract to $10.2 million for 7939 radio sets.

Prior to May, 1989, before this contract was transferred to MCLB ALBANY, GA the contractor had made significant progress early in the performance period. First article testing was conducted on time with excellent quality noted by the inspectors. The performance of the contractor in the first 180 days of the contract was sufficient to justify the exercising of the option contained in the original contract for an additional 3500 radio sets. Throughout 1987 and 1988 and until April of 1989 the contract progressed satisfactorily with minor discussions and administrative changes. The company had experienced financial difficulties throughout its history, but had performed this contract according to the

terms and conditions. Progress payments of 90% were being made based on the contract completion status.

In April of 1989 the Dallas DCAS office informed HQMC and Oklahoma Radio that deficiencies existed in the contractor's accounting system relative to isolation of cost data and recommended that progress payments be suspended until the discrepancies were resolved. The contract was transferred to MCLB Albany, GA the following month with this recommendation. Oklahoma Radio informed MCLB Albany, GA that they had changed management and reorganized to become an employee-owned firm and was eager to continue this thus far successful contract. It later became apparent that the reorganization was needed since employees had not been paid because of accounting system discrepancies that failed to isolate all costs of production resulting in no available funds to pay the employees once the manufacturing costs were met. The employees were satisfied with stock in the company in lieu of wages due. The deficiencies in the cost accounting system can be illustrated by the two examples that follow. The first is that the original manufacturer of the AN/PRC-68 radio set, Magnavox, charged the Government an average unit price of $1887 per radio set. The proposal from Oklahoma Radio contained an average unit price of $1079 per radio set. The DCAA auditors determined that the radio sets could be produced and sold under ideal manufacturing conditions for $1298 per radio set, which was the price awarded to Towson Electronics in the

original contract. Secondly, Oklahoma Radio submitted a $1.5 million claim relating to discrepancies in the technical data package, however, only $600,000 could be substantiated. The company withdrew the claim after it was audited and submitted Engineering Change Proposals (ECP) valued at only $300,000. Oklahoma Radio received the $300,000, however, the company could have resubmitted the claim to receive the previously substantiated $600,000.

Through the end of 1989 and until March of 1990 the contractor continued to deliver radio sets on a reasonably satisfactory schedule. When deliveries were discontinued after March of 1990, due to the deteriorating financial conditions, the company negotiated with several outside funding sources for financial assistance. The lack of deliveries pushed the contract into a default status in April of 1990 bringing about a series of negotiations between the Government and the contractor until May of 1991. Progress payments were not suspended until 14 May, 1991 after $7.5 million had been paid to Oklahoma Radio. The contractor had delivered 4074 of the 7939 radio sets that were due by this date. The Termination for Default notice was signed on 20 May 1991 and delivered personally to the Chief Executive Officer of Oklahoma Radio on 22 May 1991. Oklahoma Radio filed for bankruptcy on 22 May 1991. Since then, the GFE in the plant has been inventoried and containerized. The termination negotiations are still in process, however it is unlikely that

Oklahoma Radio will avoid dissolution. The loss of this minority owned small business is tragic for the employees of the company, who have no other employment opportunities in the area, and the dissolution of the company also represents a loss of a valuable source of well made equipment for the Government.

THE CAUSE OF DEFAULT IN THE TOWSON ELECTRONICS CASE

This contract failed because of indecisiveness and inaction on the part of Towson Electronics. There were some discrepancies on the part of the Government, but a proactive management team from the contractor would have been more aggressive in resolving any disparities and commencing work. This would include obtaining the necessary COMSEC materials account number and developing the quality assurance plan to the satisfaction of the QAR.

THE CAUSES OF DEFAULT IN THE OKLAHOMA RADIO CASE

This small company was unable to maintain upper level management stability throughout its history. Responsibility for financial difficulties was levied on management personnel who were relieved before having the opportunity to fully assess the deficiencies in the company's financial structure which were the root causes of insolvency.

The accounting system was inadequate because it was incapable of isolating costs associated with indirect materials and labor. Some contracts were successful, however,

the inability to properly isolate costs allocated certain costs with inappropriate contracts. This illustrates why the unit price in the original proposal was so low ($1079). The average unit price paid to Magnavox for the initial provisioning of each AN/PRC-68 radio was $1887. The $7.5 million in progress payments paid to Oklahoma Radio divided by the 4074 radio sets delivered reveals a price of $1841 per radio set paid by the Government. The company could only justify a price of $1079 per radio due to the deficient accounting system. The price of $1841 seems reasonable in relation to the Magnavox price, inflation and product improvement.

THE INDICATORS IN THE TOWSON ELECTRONICS CASE

This contract contains many obvious indicators that the firm's management was not aggressively attempting to make progress. The key indicators which should have resulted in more timely action in the administration of this contract were:

- The need to revise the attainment of the COMSEC materials account number from 45 days to 90 days
- The empty production facility 51 days after contract award
- The failure to obtain the approved quality assurance plan within the specified 30 days after contract award

- The request to obtain special tooling four months after contract award with first article testing due six months after award
- No vendor parts orders submitted upon contract award, shortly thereafter or in the ensuing four months.

THE INDICATORS IN THE OKLAHOMA RADIO CASE

In this case one of the causes of default, upper management instability, has the high turnover of personnel as its indicator. These contracts are difficult to administer and manage for an individual familiar with the case. They become virtually impossible to contend with if those who are in decision making capacity are regularly transferred to other assignments.

The accounting system deficiencies were indicated at the time the proposals were submitted. The unreasonably low proposal price should have foretold at the outset that the company may have had an ineffective system. The inability to substantiate the $1.5 million claim could also have illustrated that the firm's cost accounting system was deficient.

RECOMMENDED ACTIONS IN THE TOWSON ELECTRONICS CASE

Since this contract required expansion of the contractor's facility; the approval of a quality assurance plan and the acquisition of a COMSEC materials account number by the

contractor, more aggressive monitoring of progress on these critical milestones was necessary. Significant delays in the follow-up of the contractor's progress materially contributed to the default. Since this contract represented an entry into the field of Government contracting for the contractor, more stringent contract administration would probably have prompted appropriate progress. Had greater scrutiny not produced progress from the contractor, then an earlier termination would have been possible and the necessity to convert from a Termination for Default to a Termination for Convenience could have been avoided thereby allowing the Government to recover some of the costs associated with reprocurement.

RECOMMENDED ACTIONS IN THE OKLAHOMA RADIO CASE

Because this company had historically demonstrated the ability to produce high quality equipment, there should have been a greater effort made on part of the Government to assist Oklahoma Radio with their managerial and financial difficulties. The Small Business Administration, for example, is authorized to provide grants to 8(a) companies for managerial training. If the management had the ability to isolate the true cause of the financial difficulties to the accounting system, action would have been initiated by the company to upgrade the system, thereby halting the insidious deterioration of their financial status. The accounting system problems caused the failure of the company, but

managerial assistance would have saved it. To illustrate the cost to the Government of the failure of this company, an examination of the cost to finish the procurement of the 3865 radio sets still required is appropriate. No current source exists. Preliminary discussions with Magnavox to re-initiate production indicate a unit cost to the Government of approximately $2880. The extended price of the contract would be about $11.2 million. It is obvious that managerial training or accounting consultant services for Oklahoma Radio would have been a much more economical alternative.

D. CASES 3A AND 3B

THE REQUIREMENTS

A) The Basic Electronics Maintenance Trainer (BEMT) is a training device for electronics technicians. It is composed of a series of stations and a Trainer Central Control (TCC) unit. The system provides a self-paced study course for the student which simulates a wide variety of electronic configurations. By changing the software, the instructor can replicate malfunctions and component failures, and interject system faults to develop troubleshooting skills. The contract called for 220 individual stations and a TCC. Each station can be used without the TCC, but the software must then be individually loaded to each station and the instructor could then monitor only one student at a time.

B) The TEAMPAC Intelligence training device is a desktop simulator which provides unit and intermediate level intelligence maintenance tasks for military students. The device produces both simple and complex intelligence scenarios describing a situation to the student followed by intelligence data and a sequence of events. The student must utilize this new information to update the intelligence situation and generate new intelligence reports. Each training device is self contained and is designed to draw on the skills the students acquired during classroom and field work. The initial contract requirement called for development and prototype production.

THE CONTRACTORS

The original contractor for the BEMT was Creative Concepts, located in Holly Hills, Florida. The parent company of Creative Concepts is Wolf Technology, a large producer of radar detection devices. This contract was only the third Federal Government contract Creative Concepts had ever received. The majority of its business base was the Florida State Government and commercial firms in Florida. The primary products manufactured by the company were video disk machines and associated video disks which provided short informational and recreational program clips on a television monitor.

Ferris International, another 8(a) firm headquartered in El Segundo, California, had considerable experience in Government contracting and maintained a reputation for well

built electronic devices. The company was significantly dependant on Government contracts and required progress payments for all work to be performed. When the company was awarded the contract for the BEMT after the failure of Creative Concepts, the senior management decided to lease the building Creative Concepts had utilized and hire many of that company's former employees to perform the contract at the Holly Hills, Florida site. The TEAMPAC contract was awarded to Ferris International while the company was performing the BEMT contract. This contract was also to be performed at the Holly Hills, Florida site.

THE CONTRACTS

A) The Creative Concepts contract for the BEMT was a $2.8 million Firm Fixed Price contract to produce the 220 stations and the TCC. The contract allowed for 90% progress payments and established a delivery schedule over a two year period after contract award in November, 1986. There was no Government Furnished Equipment (GFE) associated with the contract.

The Ferris International contract for the BEMT was a $2.9 million Firm Fixed Price contract to finish the project initiated by Creative Concepts. Creative Concepts had delivered 110 of the 220 stations and had the components to produce most of the remaining 110 units and the TCC. These components were provided to Ferris International as GFE in support of the contract. The contractor's proposal was

submitted in December, 1988 and the contract was awarded in May of 1989. This new contract required some updated software and design technology which consequently required Ferris International to modify the 110 stations produced by Creative Concepts.

B) The TEAMPAC contract awarded to Ferris International was a $2 million development and prototype production Firm Fixed Price contract. The contract did not require any GFE and was considered to be a low risk venture. The development period was to last six months with a production period not to exceed 18 months following development.

THE CREATIVE CONCEPTS SITUATION

As previously mentioned above, this was only the third Federal Government contract the firm had been awarded. One of the other two contracts was with the Navy for a signals intelligence recognition device and the other was with the Air Force for a C-5 aircraft cockpit procedures trainer/simulator. The cockpit trainer contract was priced at $26 million.

The first year of the BEMT contract progressed satisfactorily with respect to the trainer stations. Near the end of the first year, however, delays in development of the TCC were encountered. The company began to experience financial difficulties associated with the C-5 contract at this time which was significantly more complex and larger than any effort entered into by the company previously. The Government took delivery of 110 of the stations but would not

accept additional stations or provide progress payments on the remaining stations until greater progress was made on the TCC. The Contracting Officer's Technical Representative (COTR) indicated to the PCO that little effort was underway on the TCC and that some of the engineers working on the project were reassigned to assist in the larger C-5 effort. Creative Concepts responded to this by indicating that the software subcontractor was late and the engineers were temporarily reassigned to avoid their becoming idle. The company also cited vague coding problems as contributing to the development delay of the TCC.

In February, 1988 DCAS warned MCLB Albany, GA that the contractor was suffering from increased financial problems and that the company's suppliers were now dealing with Creative Concepts on a cash only basis. The Naval Investigative Service (NIS) then initiated an investigation following allegations that Creative Concepts had begun applying a mark-up of subcontractor invoices by as much as 25% and passing the costs to the Government on the signals intelligence device contract. These allegations spread to the C-5 contract and consequently DCAS suspended all progress payments. Creative Concepts had received $2.2 million of the $2.8 million associated with the BEMT contract. A Cure Notice was issued in September, 1988 requiring significant progress on the TCC, but no response was provided by the company. It was clear that the company was facing serious litigation and was certain

to enter bankruptcy. The owner of Wolf Technology travelled to the Holly Hills, Florida site when he was made aware of the Cure Notice and suspended every employee on what was called a temporary basis. The owner then had the plant secured and would not make any comments regarding his actions to the ACO. Following this action, a team consisting of the contract specialist, the COTR, the program manager and his assistant went to the Holly Hills, Florida site to inventory all work-in-process items and components. The team gained access to the plant and found approximately 89% of the material necessary to complete the remaining 110 stations and about 30% of the components for the TCC. At this point (12 October 1980) the PCO at MCLB Albany, GA directed that the contract be terminated for convenience so that this material could be removed expeditiously, to avoid the massive legal action which was obviously pending. As a result of this timely action, the program was spared the excessively long delays which would have resulted from bankruptcy and fraud litigation.

THE FERRIS INTERNATIONAL SITUATION

Following the dissolution of Creative Concepts, the PCO at MCLB Albany, GA immediately solicited another contractor to satisfy the BEMT requirement. Ferris International was selected on a sole source basis under the 8(a) program and the company submitted its bid in December, 1988. Extensive negotiations were conducted regarding the updated software package and necessary modifications delaying contract award

until May of 1989. Delivery of the BEMT package was already seven months behind the original schedule.

The early progress on the BEMT was to be made on development of the TCC and the modification requirements for the existing 110 stations. Production was to begin in June of 1990 on the remaining stations.

Ferris International incurred substantial debt in its expansion effort in Florida. The bid on the BEMT and subsequently the TEAMPAC contracts reflected overhead rates which were to assist in the liquidating of this debt. Costs associated with the expansion were higher than the company expected and were higher on the Firm Fixed Price BEMT contract as well which placed the company in a tenuous financial posture beginning in July, 1989. The first indication of the financial problems at Ferris International arose when the COTR told of layoffs at the Holly Hills, Florida site of employees engaged in the development of the TCC. Delivery of technical data relating to the TCC began to fall behind schedule by late September. The DCAS Pre-award Survey of the company for the TEAMPAC contract indicated that the company was spending excessive amounts of money in management salaries and administrative costs. DCAS recommended that another source be identified because of concern that the company was going to encounter serious and long term cash flow shortages unless significant streamlining of the management and administrative structures at the company were initiated. During

negotiations, the former Vice President for Government contracts liaison at Ferris International corresponded with MCLB Albany, GA and provided as an enclosure to his letter a copy of a petition to a claims court which would force Ferris International to provide him with back pay due. The contract for the Teampac devices was awarded to Ferris International in the face of these occurrences in November, 1989.

Additional layoffs occurred throughout January, February, and March of 1990 at the Holly Hills, Florida site resulting in very limited progress on the TCC. Furthermore, no progress was made on the TEAMPAC contract. On 1 June 1990 Ferris International discontinued its lease payments on the Holly Hills, Florida site. This action did not become immediately apparent to the Government. On 15 June 1990 notice to proceed on the remaining BEMT stations was provided to Ferris International. A conference was held at the contractor's plant on 24 July 1990 to discuss progress on both the BEMT and TEAMPAC contracts. At the opening of the conference the senior representative from Ferris International announced the layoff of all the Holly Hills, Florida plant employees. A Cure Notice was provided to the home office of Ferris International in El Segundo, California on 26 July 1990 advising the company of an anticipatory breach of contract as a result of the dismissal of its employees. The company was given five days to respond, however, no response was ever received. All GFE was removed from the plant and the contract

was Terminated for Default on 8 August 1990. The contracting officer decided that a Termination for Default was required based on the determination that the facts of this case constituted anticipatory repudiation of the contract.

THE CAUSES OF DEFAULT IN THE CREATIVE CONCEPTS CASE

Creative Concepts failed for two reasons. First, the company underbid the contracts for the signals intelligence device and the C-5 cockpit procedures simulator. The firm lacked the necessary experience in dealing with the rigid requirements associated with Federal Government contracting. When the realization that they had underbid became apparent, the company resorted to fraudulent activities in attempt to diminish potential losses. Secondly, the company failed because it was saturated given the delivery schedules of the individual contracts previously awarded.

THE CAUSE OF DEFAULT IN THE FERRIS INTERNATIONAL CASE

Ferris International entered bankruptcy because of an underestimation of the cost of expansion in Florida and because of the inefficiencies in operating the business. The company simply did not have the working capital needed to maintain the necessary cash flow required to operate their newly leased facility. The management of the company failed to obtain a sufficient commercial market for their products and could not survive on the closely regulated profit margins associated with Government contracts.

THE INDICATORS IN THE CREATIVE CONCEPTS CASE

The pre-award survey of Creative Concepts should have illustrated the company's inexperience in the field of Federal Government contracting. This inexperience should have indicated that greater scrutiny of this firm was necessary.

Late delivery of any portion of a contract serves as an indicator of difficulty at any firm. The late delivery of the TCC data package, coupled with the vague excuses regarding software and coding problems is a solid indicator that the firm was experiencing a problem.

When suppliers deliver on a cash only basis and NIS initiates a fraud investigation it becomes clear that financial difficulties are present. And, although occurring late in this contract period, wholesale layoffs and plant lock-outs are clear indicators that a contractor is facing failure.

THE INDICATORS IN THE FERRIS INTERNATIONAL CASE

The failure of Ferris International was foreshadowed by various indicators. Significant dependence on Government contracts and the need for progress payments for all work should indicate a lack of available financing or working capital to meet cash flow requirements. The expansion effort represented an assumption of risk and costs by the company. The layoffs reported by the COTR; the poor results of the TEAMPAC pre-award survey and the letter from the irate Vice President, all of which occurred just prior to the TEAMPAC

award, were three sure indicators that should have signalled that Ferris was in trouble. Insufficient progress on the TCC for the BEMT contract and failure to start on the TEAMPAC contract amounted to late delivery, a common indicator of financial, technical or managerial difficulty. Wholesale layoffs in this firm again foreshadowed a pending financial disaster.

RECOMMENDED ACTIONS IN THE CREATIVE CONCEPTS CASE

Given the inexperience Creative Concepts had relative to Government contracting, an examination of the magnitude and performance of the other two contracts might have shown that the company was reaching its maximum capacity without the BEMT contract. This pre-award review action might have caused the Government to award the BEMT contract to another firm. This contract for Creative Concepts did not force the company into bankruptcy; another Government contract did. Any action taken designed to cure the late deliveries or layoffs based on this contract would probably have been immaterial in the face of the fraudulent activity which occurred. The best course of action for the Government in this case would have been to terminate as soon as the indicators pointed with some certainty that the company was in serious trouble. The Termination for Convenience in this case was particularly appropriate given the circumstances. The company had already received $2.2 million when the contract was terminated. The Government had 110 of the BEMT stations and 89% of the

required components for the other 110 in addition to the technical data and 30% of the TCC components. The simplicity of the Termination for Convenience procedure given the pending litigation and the reality that the majority of the material costs to complete the contract were already incurred, the Termination for Convenience was the most economical approach.

RECOMMENDED ACTIONS IN THE FERRIS INTERNATIONAL CASE

The Ferris International case illustrates an example similar to the Oklahoma Radio case in that financial difficulties were brought on as a result of the failure of the senior executives to recognize and correct the areas which were draining resources. In the Oklahoma Radio case the cause was the accounting system, and in this case the cause was excessive management costs and administrative inefficiency. As in the Oklahoma Radio case, had the Government provided either managerial training or managerial consultant services the company could possibly have ascertained where streamlining was needed and implemented action to reorganize the company and assure successful performance of both the BEMT and TEAMPAC contracts. Another lesson to be learned from this case is that if a company is facing significant financial difficulty in the pre-award phase of a contract, as indicated by a poor DCAS survey, employee layoffs, late deliveries, and unpaid employees, then that company should not be considered responsible enough to perform. Additional contract awards such as the TEAMPAC award are not in the best interest of

either party and only serve to delay a program until a new contractor can be found.

E. CASES 4A AND B

THE REQUIREMENTS

A) The Guardian Armor/Artillery simulator is a full crew interactive training device for both tank crews and howitzer artillery teams. The requirement in this case amounted to full scale development, prototype testing, completion of level three drawings and the submission of all associated software and life cycle cost supporting documentation.

B) The Cobra helicopter simulator is a cockpit procedures and weapon systems training device. The device provides low cost simulated flight hours and interjects random emergency situations and enemy targeting profiles. Pilots can then be evaluated on their knowledge of appropriate emergency procedures and can improve their skills in the selection and utilization of appropriate available weaponry and target engagement. The contract requirements were the same as those for the Guardian simulator.

THE CONTRACTOR

Dedalus Incorporated is an 8(a) firm headquartered in Columbia, Maryland, with an additional facility in Orlando, Florida. Dedalus Incorporated had previous experience in contracting with the Federal Government and had successfully completed work for the U.S. Army and Air Force. At the time

these contracts were awarded both the Army and Air Force had active contracts with the firm. The company was considered to be extremely competent and had produced solid electronics and software packages but did not develop a significant commercial market base.

THE CONTRACTS

A) The Guardian Armor and Artillery trainer was a $6.4 million Firm Fixed Price full scale development contract. It was awarded in September, 1987 to be completed by 1 September 1991. This contract was to be performed at the Columbia, Maryland site.

B) The Cobra helicopter simulator was a $12.6 million Firm Fixed Price full scale development contract awarded in July of 1990. Both contracts called for 90% progress payments based on percentage of work completed. This contract was to be performed at the company's plant in Orlando, Florida.

THE SITUATION

From the time the Guardian contract was awarded until January of 1991 there was no indication that the contract was in jeopardy. The development of the software and prototype trainer progressed according to the terms of the contract and in accordance with the bilaterally approved modifications negotiated during contract performance. Successful testing of the prototype occurred in December, 1990 and initial deliveries of software documentation and life cycle cost

information were made. It appeared that the contract for the Guardian would be completed by the 1 September 1991 delivery date. The performance on the Guardian contract was sufficient justification to award the Cobra contract in July, 1990 with confidence that Dedalus would satisfy both requirements. The technology was similar and some of the initial ground work for the Cobra device had been developed in the early phases of the Guardian effort.

In January, 1991 the first indications of difficulty at Dedalus began to appear. The January rental payment for the Orlando, Florida site went unpaid for 47 days until 16 February, 1991. February's rent was never paid. Validity Incorporated, one of Dedalus' largest subcontractors received its last payment on 5 January 1991 and went unpaid from Dedalus' progress payments in February, March, and April. DCMAO, Baltimore, Maryland completed a financial capability review of Dedalus on 10 March 1991 and characterized the contractor's position as marginally satisfactory based upon financial statements from 28 September 1990. In April the Internal Revenue Service indicted the owners of the firm for federal income tax evasion and indicated charges of embezzlement were pending.

Progress payments were suspended on 26 April 1991 until all audits of the company were completed by DCAA to prevent Dedalus from receiving excess payments prior to declaring bankruptcy.

The Maryland National Bank froze the company's credit line the same day and efforts on all contracts by the firm ceased. Despite these occurrences, both the Guardian and the Cobra contracts were still on schedule. The U.S. Army and Air Force contracts with Dedalus were, however, significantly delayed. The owner of Dedalus was arrested as he tried to flee the country to avoid prosecution on 9 June 1991. Two of Dedalus' largest subcontractors, Validity Incorporated and Western Computers expressed interest in purchasing Dedalus if novation of the contracts to the new owner could be accomplished. Western Computer, another 8(a) firm, provided the best offer which included completing all of Dedalus' 8(a) contracts, hiring Dedalus' employees, buying Dedalus' accounts receivable and acquiring certain assets of Dedalus. 13 CFR 124.317(a) states "...a contract (including options) awarded pursuant to section 8(a) of the Small Business Act...shall be performed by the concern that initially received such contract. If the owner upon...whom eligibility was based relinquishes ownership or control...of such concern...such contract or option shall be terminated for the convenience of the Government." 13 CFR 124.317(d) also states "A procuring agency may request a waiver of the requirements of paragraph (a) of this section if the head of the procuring agency certifies that termination of the contract would severely impair attainment of the agency program objectives or missions." MCLB Albany, Georgia provided the certification in their request for waiver to the

SBA in a letter dated 18 July 1991. The results of the letter, the novation procedure and the outcome of these two contracts are currently pending. All indications suggest that Western Computer will receive the contracts and control of Dedalus Incorporated and will complete them in a reasonable time frame.

THE CAUSE OF DEFAULT

This company failed because of the owner's embezzlement of funds. The firm had the technical, managerial and financial resource to complete all the contracts it had been awarded. As the owner began his criminal activity, the financial posture of the firm began to erode. The company was not able to maintain solvency as a result of this drain of resources.

THE INDICATORS

The firm had been performing very well up until nine months before its failure. The indications that difficulties were being encountered began with the marginal financial statements in September, 1990. The unpaid rent on the Orlando, Florida plant; the cessation of payments to subcontractors and the IRS indictment followed, all of which pointed to the eventual failure of the company.

RECOMMENDED ACTIONS

The audit of financial statements for 8(a) firms should not require six months time. If the DCMAO financial capability review had been performed in a more timely manner,

the contracting officer would have been aware of the deteriorating financial position of Dedalus Incorporated much earlier. The contracting officer was not aware of the unpaid rent or the failure to pay subcontractors until mid-April when it was too late to take any effective action. Had the contracting officer been aware of the marginal financial statements, closer scrutiny of the company's financial dealings would have resulted which would have led to the discovery of the other indicators of financial trouble. If these indicators been discovered when they occurred, progress payments could have been suspended earlier thereby saving money for the Government. When the contractor fails due to criminal activity, it is difficult to implement actions to assist the company. Early action in the administration of contract performance, however, will same time and money.

IV. THE 8(A) PROGRAM SURVEY RESULTS

The contracting officers and small business advocates at the 10 United States Marine Corps contracting offices were surveyed to assist in this research effort during April and May of 1991 relative to the primary causes of 8(a) firm failure/contract default; the key indicators of the difficulties leading to failure/default and the steps which the Government should reasonably have taken to alleviate these difficulties. The information obtained from these responses provides valuable insight in the administration of 8(a) contracts.

The survey indicated that the most common causes of 8(a) contract default are, in order from most common to least common: insufficient working capital, lack of technical expertise, inexperienced/poor management and lack of knowledge regarding dealing with Government requirements. Other causes listed were: inadequate accounting systems, poor estimating systems, poor staffing and the collapse of the firm when required to assume a greater percentage of non-8(a) business.

The following table illustrates the number of times each cause was listed by those who responded to the survey. Twenty questionnaires were sent out. All went to the ten U. S. Marine Corps contracting offices. Ten were sent to the contracting officers and ten were sent to the small business

advocates. Their responses were extremely similar indicating that little bias existed toward the program from either set of individuals. Six of the twenty individuals surveyed were non-responsive.

TABLE II
CAUSES OF DEFAULT

CAUSE	# CITING CAUSE
INSUFFICIENT WORKING CAPITAL	13
LACK OF TECHNICAL EXPERTISE	10
INEXPERIENCED/POOR MANAGEMENT	8
POOR KNOWLEDGE IN DEALING WITH GOVERNMENT	5
POOR ESTIMATING SYSTEMS	2
INADEQUATE ACCOUNTING SYSTEM	2
POOR STAFFING	1
INABILITY TO SURVIVE WITHOUT HIGH % OF GOVERNMENT WORK	1

These causes of failure warrant closer scrutiny to illustrate the indications which can be observed during contract administration that signal difficulties are being encountered which could lead to default and the steps which should reasonably be taken by the Government to relieve the difficulties thereby preventing default. It should be noted that every respondent to the survey indicated that the majority of the problems encountered with 8(a) contracts could have been avoided had the SBA conducted adequate pre-award actions to correct contractor's material deficiencies or disqualify the contractor due to incapability of performance of a particular contract without improvement in one or more critical areas of the company.

An examination of these causes of failure follows to provide insight and recommended steps to improve dealings with 8(a) firms as described by the respondents to the survey. The title heading refers to the cause of default or firm failure. The column of indicators provides events or observations evident during contract administration which can diagnose a potential cause of failure or default. The "number citing indicator" column refers to the number of surveys received which noted this indicator as associated with the cause of failure or default. The steps to alleviate difficulties are measures contracting officers can take to prevent default for the particular cause.

TABLE III
INSUFFICIENT WORKING CAPITAL

INDICATOR	# CITING INDICATOR
REQUESTS FOR ADVANCE PAYMENTS	7
REQUESTS FOR UNUSUAL PROGRESS PAYMENTS	4
INABILITY TO HANDLE CONTRACT GROWTH	3
DELAY IN PROCURING MATERIALS	2
UNUSUAL REQUESTS FOR GFE	1
COMPANY HAS POOR RATING WITH CREDITORS	1
COMPANY HAS HIGH DEBT TO EQUITY RATIO	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
BETTER PRE-AWARD SURVEY	13
PROVIDE ADVANCE PAYMENTS TO SOLID FIRMS	7
PROVIDE TIMELY PROGRESS PAYMENTS	5
PROVIDE UNUSUAL PROGRESS PAYMENTS	4
INSTITUTE CLOSE FINANCIAL MONITORING	2
PROVIDE FINANCIAL MANAGEMENT TRAINING	2
EXERCISE LENIENCY IN PRICING ADJUSTMENTS	1
LIMIT GROWTH IN CONTRACT TO A PERCENTAGE	1

TABLE IV
LACK OF TECHNICAL EXPERTISE

INDICATOR	# CITING INDICATOR
REQUESTS FOR EXTENSIONS	5
FIRST ARTICLE TEST FAILURE	3
DIFFICULTY RESPONDING TO CHANGES	3
LACK OF CREDENTIALS FOR ENGINEERS	2
ENGINEERS NOT FAMILIAR WITH STATE-OF-THE-ART	1
INCOMPLETE TECHNICAL REPORTS	1
COST OVERRUNS	1
HIGH ENGINEERING PERSONNEL TURNOVER	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
BETTER PRE-AWARD SURVEY	7
ACCURATELY CLASSIFY A FIRM'S CAPABILITIES	3
LIMIT CHANGES AS MUCH AS POSSIBLE	2
ALLOW EXTENSIONS IF POSSIBLE	2
TERMINATE CONTRACT EARLY WHEN DEFAULT IS INEVITABLE TO PREVENT LARGER LOSSES	2

TABLE V
INEXPERIENCED/POOR MANAGEMENT

INDICATOR	# CITING INDICATOR
MANAGERS LACK FORMAL TRAINING/DEGREES	5
FAMILY MEMBERS MANAGE MOST/ALL OF FIRM	3
HIGH MANAGERIAL TURNOVER	2
MANAGER HAS WORKED IN OTHER FAILED 8(A) FIRMS	1
EMPLOYEES INDICATE DISSATISFACTION WITH MANAGEMENT	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
BETTER PRE-AWARD AUDIT OF MANAGEMENT	7
PROVIDE MANAGEMENT TRAINING AT GOVERNMENT EXPENSE	4
REQUIRE MANAGEMENT TRAINING AT CONTRACTOR EXPENSE	2
RECOMMEND MILESTONE PLAN FOR CONTRACT PERFORMANCE	1

TABLE VI
LACK OF KNOWLEDGE REGARDING
DEALING WITH GOVERNMENT REQUIREMENTS

INDICATOR	# CITING INDICATOR
INADEQUATE REPORTING OF CONTRACT STATUS	3
CONTRACTOR HAS DIFFICULTY UNDERSTANDING COMMON CLAUSES IN CONTRACT	3
CONTRACTOR NOT FAMILIAR WITH TINA	1
CONTRACTOR SURPRISED BY GOVERNMENT ABILITY TO MAKE UNILATERAL CHANGES	1
CONTRACTOR NOT FAMILIAR WITH FAR	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
BETTER PRE-AWARD SURVEY	4
MINIMIZE ADMINISTRATIVE REQUIREMENTS	2
PROVIDE PRE- AND POST-AWARD CONFERENCES TO ASSIST CONTRACTOR	2
PROVIDE TRAINING IN GOVERNMENT REQUIREMENTS	2

TABLE VII
POOR ESTIMATING SYSTEMS

INDICATOR	# CITING INDICATOR
DELINQUENT DELIVERY	2
REQUESTS FOR DELIVERY EXTENSION	1
VENDOR REPORTS DO/DX ORDERS TOOK PRECEDENCE AND DELAYED DELIVERY	1
COST OVERRUNS	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
BETTER PRE-AWARD EXAMINATION OF ESTIMATING SYSTEM	2
FORCE FIRM TO FULLY SUBSTANTIATE ESTIMATES PRIOR TO AWARD AND FOR CHANGES	2
MAKE CONSULTING SERVICES AVAILABLE TO CONTRACTOR TO IMPROVE HIS ESTIMATING SYSTEM	1

TABLE VIII
INADEQUATE ACCOUNTING SYSTEM

INDICATOR	# CITING INDICATOR
LACK OF DATA TO SUPPORT COST PROPOSALS	2
DIFFICULTY IN RETRIEVING SIMPLE COST INFORMATION	1
IMPROPER OVERHEAD ALLOCATION TECHNIQUES	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
PROVIDE CONSULTANT TO UPGRADE ACCOUNTING SYSTEM	1
IMPROVED PRE-AWARD SURVEY OF ACCOUNTING SYSTEM	1

TABLE IX
POOR STAFFING

INDICATOR	# CITING INDICATOR
LONG DELAYS IN RESPONDING TO ADMINISTRATIVE REQUESTS OR CHANGE REQUESTS	1
RELIANCE ON ONE/FEW INDIVIDUALS FOR ALL DECISIONS	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
RELAX DEMANDS WHICH REQUIRE SPECIALIZED RESPONSE	1
ALLOW MORE TIME FOR RESPONSES FROM CONTRACTOR	1
PROVIDED PERSONNEL MANAGEMENT CONSULTING	1

TABLE X
INABILITY TO SURVIVE WITHOUT A
HIGH PERCENTAGE OF GOVERNMENT CONTRACTS

INDICATOR	# CITING INDICATOR
MOST OR ALL WORK WITH THE GOVERNMENT	1
SBA HAS COUNSELLED CONTRACTOR ON SHORTFALL IN MEETING NON-8(A) CONTRACT REQUIREMENTS	1

STEPS TO ALLEVIATE DIFFICULTIES	# CITING STEP
DETERMINE GOVERNMENT RELIANCE DURING PRE-AWARD SURVEY	1
TRY TO ILLUSTRATE COMMERCIAL APPLICATIONS FOR CURRENT GOVERNMENT WORK	1

V. *CONCLUSION AND RECOMMENDATIONS*

A. *CONCLUSIONS*

In addition to the information relative to causes and indicators of default and the steps to preclude them, the survey solicited information regarding the benefits associated with the 8(a) program. The benefits most commonly listed were:

- THE PROGRAM EXPANDS THE INDUSTRIAL BASE
- CONTRACTS CAN BE AWARDED VERY RAPIDLY UNDER THE PROGRAM
- THE PROGRAM PROVIDES EMPLOYMENT IN DEPRESSED AREAS
- THE PROGRAM INCREASES COMPETITION BY ASSISTING NEW BUSINESS

These benefits can become valuable assets to the contracting officer. They cannot be realized if the contractor does not deliver the goods however. As indicated in Chapter II, the SBA is not adequately staffed to perform all the required services relative to managing the 8(a) program. One significant shortcoming is the inability to perform comprehensive pre-award actions. The only recourse available to the contracting officer is to deal with the contractor's particular situation in the post-award phase. The key to successful contract actions with 8(a) firms is the ability to recognize the indicators that firms are facing difficulties in contract performance and to act to alleviate these difficulties in a reasonable and responsible manner.

It is clear that this thesis does not completely enumerate the causes of default on the part of 8(a) firms. It does not provide a collectively exhaustive list of indicators of difficulty, nor can it serve as a comprehensive "what-to-do-when" guide for contract administration. The information contained in this thesis does, however, indicate what some of the primary causes of 8(a) contract default and 8(a) firm failure are, and that they can be diagnosed before it is too late through key indicators that the contracting officer can easily observe. The steps to alleviate the difficulties leading to default which are provided in the thesis are examples of relatively simple yet economically significant measures which will result in greater success when dealing with 8(a) companies. The contracting officer must be alert for unusual conditions, actions or omissions on the part of the contractor and be aware that observable indicators exist which may signal future difficulties. Just as each element of a contract has meaning and cannot be excluded or interpreted in a manner which renders it inconsequential, each action or failure to act on the part of the contractor has meaning relative to the performance of a particular contract or to the condition of company in general. These actions or failures to act on the part of the contractor can be utilized by the contracting officer as indicators of potential difficulties which may be encountered by the contractor which could

ultimately jeopardize the completion of the contract or foreshadow the failure of the firm.

B. *RECOMMENDATIONS*

Each contracting officer will have to determine what action is appropriate in response to an indication that some difficulty is to be encountered in contract performance. The examples of recommended actions contained in this thesis provide measures which in hindsight, may have prompted success instead of failure for an 8(a) firm. There are other approaches which could be taken which might alleviate the difficulties, as well as, or better than those provided. The single most important recommendation for each case is to take some form of action as early as possible. Small problems tend to become extremely large and deficiencies which would be relatively easy to correct in early stages become exacerbated over time. Insidious problems like the Oklahoma Radio accounting system shortcomings cause a misdiagnosed deterioration of a company until it collapses. Missed milestones or delivery dates must be aggressively investigated upon occurrence. Layoffs, disgruntled creditors and unpaid employees indicate financial or managerial difficulties which could be alleviated using the assistance available from the SBA under the 8(a) program or from the contracting officer. With this attitude in mind, the contracting officer can efficiently examine selected aspects of a firm in a timely

manner and act to correct deficiencies thus promoting success in contracting with minority owned firms.

C. RECOMMENDATIONS FOR FURTHER STUDY

The following areas should be studied to more accurately determine the role and responsibility the Government should assume relative to insuring successful 8(a) contract actions and the survival of 8(a) firms:

- An analysis of the requirements the Government must satisfy in monitoring 8(a) firms compared with the number of employees assigned these duties at the SBA and the number of 8(a) firms requiring monitoring to determine the feasibility and reasonableness of the current statutes governing the 8(a) program.
- A study which attempts to more thoroughly catalog the relationship between occurrences or circumstances recognized during contract performance and their root causes which would serve as a management tool for contract administrators to illustrate how these occurrences and circumstances can indicate where difficulties in contract performance are occurring.

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